

Message Text

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CIEP-01 COME-00 DODE-00 EB-07 FPC-01 H-02 INR-07

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PRS-01 /093 W

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FM AMEMBASSY CARACAS

TO SECSTATE WASHDC 8556

C O N F I D E N T I A L SECTION 1 OF 2 CARACAS 4471

EO 11652: GDS

TAGS: ENRG EINV VE

SUBJ: PETROLEUM REVERSION BILL - SOME KEY CHANGE LIKELY

REF: A. CARACAS 2874 B. CARACAS 2963

BEGIN SUMMARY. APART FROM ANY AMENDMENTS THAT CONGRESS MAY PROPOSE TO THE DRAFT OIL REVERSION BILL, THERE ARE STRONG INDICATIONS THAT THE GOV WILL MAKE AT LEAST TWO KEY CHANGES REGARDING THE GUARANTEE FUND REQUIREMENT AND THE SUPERVISORY COMMISSION. THE FIRST CHANGE IS IN RECOGNITION OF PRIVATE OIL COMPANY OPPOSITION TO HAVING TO PAY IN LARGE SUMS OF MONEY AT THE SAME TIME THEIR ASSETS ARE BEING NATIONALIZED, AND THE LATTER CHANGE IS BASED ON GOV BELIEF THAT AN INTERIM MANAGING BODY IS NOT NEEDED AND WOULD ONLY COMPLICATE THE NATIONALIZATION PROCESS. WITH RESPECT TO POSSIBLE ELIMINATION OF THE CONTROVERSIAL ARTICLE 5, THE GOV IS HOLDING FIRM IN ITS OPINION THAT THE ARTICLE IS ESSENTIAL TO THE EFFICIENT OPERATION OF THE INDUSTRY AFTER NATIONALIZATION. END SUMMARY

2. ALMOST FROM THE DAY THE DRAFT OIL REVERSION BILL WAS HANDED TO CONGRESS, THERE HAVE BEEN REPORTS IT WOULD BE FURTHER AMENDED
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BY THE GOV. THESE REPORTS HAVE BEEN SUPPORTED BY COMMENTS

FROM SO MANY AUTHORITATIVE SOURCES THAT THE EMBASSY BELIEVES IT APPROPRIATE TO INDICATE THE LIKELIHOOD THAT THEY WILL BE IMPLEMENTED. INDEED, ONE WELL-PLACED MINISTRY OF MINES AND HYDROCARBONS SOURCE HAS STATED THAT IT WILL BE DIFFICULT TO RECOGNIZE THE SIMILARITY BETWEEN THE PRESENT DRAFT VERSION OF THE LAW AND THE ONE THAT WILL FINALLY EMERGE.

2. THE KEY CHANGE WILL BE THE ELIMINATION OF THE GUARANTEE FUND REQUIREMENT (ARTICLE 19) IN ITS PRESENT FORM. AS DIFFICULT AS IT MAY BE TO COMPREHEND, THE INCLUSION OF ARTICLE 19 IN THE DRAFT PRESENTED TO CONGRESS WAS APPARENTLY DUE TO AN ADMINISTRATIVE ERROR ON THE PART OF THE MINISTRY. SOURCES REPORT THAT THE REMOVAL OF THE GUARANTEE FUND REQUIREMENT WAS ONE OF THE ITEMS WHICH PRESIDENT PEREZ DID DISCUSS WITH EX-PRESIDENT CALDERA, AND AN AGREEMENT WAS REACHED BETWEEN THE TWO POLITICAL PARTY LEADERS THAT THE FUND WAS NOT NECESSARY. MINES MINISTRY TECHNICIANS WERE ALSO ADVISING THAT OIL COMPANIES WOULD BE STUBBORN ON THIS POINT. THE REQUIREMENT FOR OIL COMPANIES TO BRING IN NEARLY \$500 MILLION WITHIN 30 DAYS TO BRING THE FUND UP TO 10 PERCENT OF ACCUMULATED GROSS INVESTMENT WOULD BE DIFFICULT TO ENFORCE. THIS WOULD BE ESPECIALLY TRUE IF THE DECISION WAS MADE TO PAY COMPENSATION TO THE OIL COMPANIES IN BONDS RATHER THAN CASH. THUS, ORDERS WERE GIVEN FOR ARTICLE 19 TO BE TAKEN OUT. THE CABINET WAS REPORTED TO BE UPSET TO FIND THE ARTICLE STILL INCLUDED WHEN IT MET FOR A FINAL REVIEW OF THE BILL ON MARCH 11, THE DAY THE MINISTER OF MINES AND HYDROCARBONS WAS SCHEDULED TO HAND IT TO CONGRESS. SINCE THERE WAS NO TIME LEFT TO REPRINT THE BILL BEFORE GIVING IT TO CONGRESS LATER IN THE DAY, THE DECISION WAS TAKEN TO SEND THE BILL AS IT WAS AND REMOVE THE ARTICLE DURING THE CONGRESSIONAL REVIEW. THE BILL HAD TO GO TO CONGRESS ON THAT DATE SINCE THE PRESIDENT WOULD BE DELIVERING HIS ANNUAL REPORT TO CONGRESS, IN WHICH HE DEFENDED HIS AMENDMENTS TO THE BILL, ON THE FOLLOWING MORNING. AS A SIDELIGHT, THERE IS SPECULATION THAT ONE OF THE REASONS WHY THE DIRECTOR GENERAL OF MINES AND HYDROCARBONS, FERNANDO BAEZ, WAS FIRED SHORTLY THEREAFTER WAS BECAUSE IT WAS HIS RESPONSIBILITY TO COORDINATE THE MINISTRY'S DRAFTING OF THE REVISED BILL. SINCE HE DID NOT CARRY OUT THE ORDER TO ELIMINATE THE ARTICLE, FOR WHATEVER MOTIVE, HE WAS FIRED.

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3. MINISTER OF MINES AND HYDROCARBONS VALENTIN HERNANDEZ BEGAN HIS SECOND ROUND OF TALKS WITH BOTH CREOLE PETROLEUM AND SHELL BY ADMITTING THAT THE INCLUSION OF ARTICLE 19 IN THE DRAFT BILL SENT TO CONGRESS WAS A MISTAKE. BOTH COMPANIES HAVE SEPARATELY STATED THIS TO EMBASSY OFFICIALS. A NEWS-PAPER STORY, OBVIOUSLY PLANTED BY THE MINISTRY, SPECULATED SHORTLY AFTER THE DRAFT LAW WAS PRESENTED TO CONGRESS THAT THE GUARANTEE FUND REQUIREMENT, IN ITS PRESENT FORM, WOULD

BE ELIMINATED DURING THE CONGRESSIONAL REVIEW. A SENIOR OFFICIAL OF THE MINISTRY TOLD THE EMBASSY PETROLEUM ATTACHE THAT THE STRATEGY WILL BE FOR THE PRESIDENT OF CONGRESS, GONZALO BARRIOS, TO INTRODUCE THE AMENDMENT AFTER THE PUBLIC HEARINGS OF THE HYDROCARBONS COMMISSION ARE COMPLETED.

4. THE MINISTRY OF MINES AND HYDROCARBONS DIRECTOR OF REVERSION, HUMBERTO CALDERON, DESCRIBED TO THE PETROLEUM ATTACHE HOW THE AMENDMENT WILL BE EFFECTED. CALDERON SAID THAT IN LIEU OF THE OIL COMPANIES HAVING TO BRING IN FUNDS TO BUILD UP THEIR GUARANTEE COMMITMENT, THE GOV WILL PLACE THE FIRST THREE YEARS OF COMPENSATION BONDS INTO A NON-NEGOTIABLE TRUST ARRANGEMENT. THE BONDS COULD THEN BE DRAWN ON THE GOV IN THE SAME MANNER AS A GUARANTEE FUND FOR ANY OBLIGATIONS THAT MIGHT BE OWED THE STATE THAT

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C O N F I D E N T I A L SECTION 2 OF 2 CARACAS 4471

WERE NOT PREVIOUSLY DEDUCTED FROM THE AMOUNT OF COMPENSATION DUE TO THE COMPANIES. THIS PLAN CLEARLY INDICATES THAT THE GOV INTENDS TO PAY COMPENSATION TO THE OIL COMPANIES IN BONDS RATHER THAN IN CASH.

5. THERE IS NO ASSURANCE THAT THIS ARRANGEMENT WILL BE MORE SATISFACTORY TO THE OIL COMPANIES THAN THAT CONTAINED IN THE

PRESENT DRAFT BILL. THE OIL COMPANIES OBVIOUSLY PREFER TO BE PAID COMPENSATION IN CASH, AND THEY PREFER TO NEGOTIATE THE AMOUNT OF COMPENSATION RATHER THAN BE TOLD BY THE GOV HOW MUCH IT WILL BE. BUT THE PROPOSED ELIMINATION OF THE OBLIGATION FOR THE COMPANIES TO BRING IN MONEY TO BUILD UP A GUARANTEE FUND REPRESENTS A CONCESSION ON THE PART OF THE GOV. IT INDICATES A WILLINGNESS TO NEGOTIATE A COMPROMISE, WHICH MUST BE VIEWED AS SALUTARY.

6. THE SECOND CHANGE CONTEMPLATED IS THE AMENDMENT OF ARTICLE 9 CONCERNING THE ESTABLISHMENT OF AN INTERIM SUPERVISORY COMMISSION. MINISTRY OF MINES AND HYDROCARBONS TECHNICIANS, AS WELL AS MANY OTHER OIL AUTHORITIES IN VENEZUELA, BELIEVE THAT IT WOULD BE IMPRACTICAL TO ESTABLISH A SUPERVISORY COMMISSION, WITH ALL THE DELAY AND BUREAUCRATIC IMPLICATIONS IT CONFIDENTIAL

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WOULD ENTAIL. THEY BELIEVE THAT PRIORITY SHOULD BE GIVEN TO SETTING UP THE HOLDING COMPANY THAT WOULD TAKE OVER FROM THE SUPERVISORY COMMISSION IN ANY EVENT. THEREFORE, TO AVOID CONFUSION, DUPLICATION OF WORK, AND DELAY, THE MINISTRY WILL PROPOSE THAT ITS PERSONNEL STAFF THE COMMISSION. SINCE THEY ARE INTIMATELY FAMILIAR WITH OIL INDUSTRY OPERATIONS, THEY BELIEVE THERE WOULD BE NO HITCH IN THE TRANSITION PERIOD UNDER THEIR PROPOSAL. IN ORDER TO GIVE THE COMMISSION AN APPEARANCE OF BROADER REPRESENTATION, SOME OIL COMPANY OBSERVERS MIGHT ALSO BE APPOINTED. THIS PROPOSED CHANGE HAS BEEN PUBLICLY ENDORSED BY AGROPET, THE LARGE ASSOCIATION OF VENEZUELAN OIL INDUSTRY TECHNICIANS, IN TESTIMONY BEFORE THE HYDROCARBONS COMMISSION OF CONGRESS.

7. REGARDING ARTICLE 5, WHICH HAS BEEN THE FOCAL POINT OF POLITICAL CONTROVERSY BECAUSE IT WOULD PERMIT PRIVATE OIL COMPANY PARTICIPATION IN MIXED COMPANIES WITH THE STATE AFTER NATIONALIZATION, THE PEREZ ADMINISTRATION IS STANDING FIRM IN DEFENSE OF THE NECESSITY FOR THIS PROVISION. MINISTRY OF MINES OFFICIALS TESTIFIED BEFORE CONGRESS ON APRIL 22 AND ELABORATED ON THE NEED FOR THE RETENTION OF THIS ARTICLE. IN ADDITION TO THE STANDARD ARGUMENTS PUT FORTH FOR OIL COMPANY EXPERTISE IN INTERNATIONAL MARKETING AND TECHNOLOGY, A MINISTRY OFFICIAL MADE THE POINT THAT ARTICLE 5 WOULD ALLOW VENEZUELA TO CREATE A COMPLEX OF OIL REFINERIES, INCLUDING AMUAY, MORON, CARDON - AND ARUBA AND CURACAO - THAT WOULD BE THE LARGEST IN THE WORLD. THE OFFICIAL WAS SIGNALING THE AREA IN WHICH MOST AUTHORITIES BELIEVE THE GOV WOULD AGREE TO MIXED COMPANIES -- REFINING. GOV OFFICIALS REALIZE THAT, IN ORDER TO CARRY OUT LARGE SCALE IMPROVEMENTS IN THE LOCAL REFINING INDUSTRY, THEY WILL PROBABLY HAVE TO PERMIT THE PRIVATE OIL COMPANIES TO RETAIN SHARES IN THEIR REFINERIES AFTER NATIONALIZATION IN ORDER TO OBTAIN THEIR COOPERATION.

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